

**Q. Please provide the change in the 2006 forecast income tax impact, if any, under the scenario where no portion of the unbilled revenue was recognized to offset the increased 2006 depreciation expense and instead the Company was permitted to defer an amount of depreciation expense equivalent to the “true up adjustment”?**

**A.** Under the scenario proposed (the “Depreciation Deferral Scenario”), Newfoundland Power would recognize \$3,086,000 of the accrued revenue for regulatory purposes. Under the Depreciation Deferral Scenario, forecast income tax expense for 2006 would increase by approximately \$1.7 million.

Attachment A provides the Company’s forecast 2006 financial results comparing proposals contained in the 2006 Accounting Policy Application to the Depreciation Deferral Scenario suggested in this Request for Information.

The comparative impacts are summarized in Table 1.

**Table 1**  
**Forecast 2006 Impacts**  
**Newfoundland Power Proposal vs. Depreciation Deferral Scenario**

	<b>Newfoundland Power Proposal</b>	<b>Depreciation Deferral Scenario</b>
Rate of Return on Rate Base	8.56%	8.19%
Regulated Rate of Return on Book Equity	9.24%	8.41%

Under the Depreciation Deferral Scenario, Newfoundland Power’s forecast 2006 rates of return are (i) lower than calculated under the Newfoundland Power proposal and (ii) below currently recognized just and reasonable rates of return.<sup>1</sup> As a result, the Depreciation Deferral Scenario would not provide the opportunity for Newfoundland Power to earn a just and reasonable return on rate base in 2006.

The Depreciation Deferral Scenario could result in Newfoundland Power accelerating its planned 2007 general rate application (“GRA”) in order to address a forecast 2006 revenue shortfall in 2006. Practically, this might result in Newfoundland Power requesting a rate increase to be implemented in the fall of 2006 to recover the additional revenue necessary to earn a just and reasonable return in 2006. It is uncertain whether a GRA process to implement revised rates in 2006 is feasible. Accordingly, the Depreciation Deferral Scenario would tend to create uncertainty in 2006 with respect to both (i) Newfoundland Power’s financial and operational plans and (ii) customer rates.

<sup>1</sup> The approved rate of return on rate base is currently 8.68%, in a range of 8.50% – 8.86%. The 8.68% rate of return on rate base is based upon a rate of return on common equity of 9.24%.

**Newfoundland Power Inc.**

**2006 Forecast**

**Newfoundland Power Proposal vs. Depreciation Deferral Scenario  
(000s)**

	<b>Newfoundland Power Proposal<sup>1</sup></b>	<b>Depreciation Deferral Scenario<sup>2</sup></b>
1		
2		
3	Billed Revenue \$ 417,069	\$ 417,069
4	2006 Unbilled Revenue Accrual 457	457 <sup>3</sup>
5	2005 Unbilled Revenue Accrual 9,579	2,629 <sup>3</sup>
6	427,105	420,155
7	Purchased Power Expense 265,498	265,498
8	Contribution 161,607	154,657
9		
10	Other Revenue 9,950	9,950
11		
12	Other Expenses:	
13	Operating Expenses 54,153	54,153
14	Depreciation 39,079	33,286
15	Finance Charges 32,637	32,637
16	125,869	120,076
17		
18	Income Before Income Taxes 45,688	44,531
19	Income Taxes 15,335	17,034
20		
21	Net Income 30,353	27,497
22	Preferred Dividends 591	591
23		
24	Earnings Applicable	
25	to Common Shares \$ 29,762	\$ 26,906
26		
27		
28	<b>Rate of Return Metrics</b>	
29		
30	Regulated Return on Book Equity 9.24%	8.41%
31	Rate of Return on Rate Base <sup>4</sup> 8.56%	8.19%

<sup>1</sup> See Exhibit NP-14, Page 1 of 5.

<sup>2</sup> Assumes recognition of revenue for regulatory purposes based on the accrual method and all consequential matters as detailed in the 2006 Accounting Policy Application adjusted to reflect the Board's request for information.

<sup>3</sup> The total accrual of \$457,000 and \$2,629,000 equals the \$3,086,000 tax expense associated with the income tax settlement.

<sup>4</sup> In Order No. P.U. 50 (2004), Newfoundland Power's rate of return on rate base, used to set customer rates for 2005, was approved at 8.68% in a range of 8.50% to 8.86%.